The Inflation Reduction Act (IRA) was signed into law on August 16, 2022. The key components of the legislation include new corporate taxes, climate initiatives, additional funding for the Internal Revenue Service (IRS), and healthcare provisions. The full package includes over $250 billion in green energy tax credits, tax incentives for electric vehicles, and funding for climate and consumer energy initiatives. It also provides subsidies for Affordable Care Act health insurance coverage, seeks to reduce Medicare spending on drugs, and restructures the Medicare Part D program to reduce the out-of-pocket cost to beneficiaries. This article provides a broad overview of the key provisions.

Tax Provisions

The IRA contains several new, reinstated, or extended tax provisions.

Corporate Minimum Tax

By far the biggest tax revenue raiser included in the legislation is the long-discussed corporate minimum tax, which the Joint Committee on Taxation (JCT) estimates will bring in over $222 billion over the course of the 10-year budget period. This provision imposes a 15% minimum tax on "book income" for C corporations with average "book income" greater than $1 billion over a three-year period. Once a corporation meets the income test to make this provision applicable, it remains subject to the corporate minimum tax in subsequent years unless it meets certain exceptions. This tax will be effective for tax years beginning after December 31, 2022.

The final legislation included some changes to this provision from the original proposal. Notably, it now allows adjustments to "book income" to reflect approved tax accounting methods to calculate depreciation rather than using book depreciation. Additionally, a provision that would have grouped together additional entities for the purpose of determining whether a company meets the applicability threshold (including private equity funds) was removed from the final bill.

While there are concerns by the accounting profession regarding both the appropriateness and complexity of determining taxes based on financial statement income derived from application of generally accepted accounting principles rather than tax-basis accounting, this provision is expected to impact a very small number of companies (less than 150) based on the current thresholds. However, the broader concern is whether the threshold could be lowered in future years in order to generate more tax revenue, now that the law is in place. Application of this provision with lower thresholds would have greater implications.

Excise Tax on Repurchase of Corporate Stock

The JCT estimates the excise tax of 1% on the fair market value of stock repurchased by public companies will generate $73.7 billion over the 10-year period. This tax is imposed on stock buy-backs by publicly traded U.S. companies as well as any subsidiary that has at least 50% of its stock owned by a corporation and will apply to stock repurchases after December 31, 2022.

The legislation allows certain exemptions, including tax-free reorganizations and stock repurchases with a total value of $1 million or less during the applicable tax year.

Extension of Limitation on Excess Business Losses

The Tax Cuts and Jobs Act of 2017 imposed an excess business loss limitation for noncorporate taxpayers. This provision limits the deduction for losses from trades or businesses in excess of $250,000 for individuals or $500,000 for married filing a joint return, adjusted for inflation. Business losses in excess of the allowable amount are carried forward to the subsequent tax year as a net operating loss.

This provision was scheduled to sunset after December 31, 2025. The American Rescue Plan Act of 2021 extended the limitation for an additional year (through December 31, 2026) after the CARES Act repealed the limitation for 2018, 2019, and 2020. The IRA now extends this limitation for an additional two years, such that it will remain in effect through 2028 (tax years beginning before January 1, 2029). The JCT estimates this extension will raise $52.8 billion.

Other Taxes

The IRA reinstates the Superfund Hazardous Substance Financing Rate, which is applied to crude oil and imported petroleum products at a rate of 16.4 cents per gallon, adjusted for inflation. This provision is effective January 1, 2023 and is estimated to raise $11.7 billion according to the JCT.

Additionally, the legislation permanently extends the temporarily increased rate of the coal production excess tax to fund the Black Lung Disability Trust Fund. This extension applies to sales in calendar quarters beginning after the date of enactment (i.e., fourth quarter 2022). JCT estimates this will raise an additional $1.16 billion.

What's Not Included?

Several provisions that had previously been proposed were removed leading up to the final Congressional votes on the IRA legislation. These include:

- **Carried interest** – The provision that would have eliminated the carried interest provision that allows a 20% tax rate on income for private equity, hedge fund, and other investment managers was removed from the final bill.
- **State & Local Tax (SALT) deduction limit** – Many Congressional Democrats pushed for the $10,000 limit on the deduction for state and local taxes to be raised, and at one point indicated they would not vote for a bill without a "SALT fix." In the end, the IRA did not make any changes to the current SALT limit.

Tax Credits and Incentives

The legislation includes a variety of tax credits, mostly to incentivize activity in connection with climate initiatives.

Credits available to individuals include the following (with budget impact amounts as estimated by JCT):

- **Clean vehicle credit** ($7.5 billion) – Provides a credit of up to $7,500 for qualified "clean" vehicles (electric or fuel cell vehicles) acquired January 1, 2023 through December 31, 2032. The credit is not allowed if the lesser of the modified adjusted gross income (MAGI) for the current or immediately preceding tax year exceeds $300,000 (joint return/surviving spouse), $225,000 (head of household), or $150,000 (individual), as applicable. The MSRP of the applicable vehicle also must exceed certain thresholds. Additionally, there are restrictions pertaining to critical minerals and battery components sourced outside of the U.S.
- **Pre-owned clean vehicle credit** ($1.3 billion) – Allows a credit of the lesser of $4,000 or 30% of the sales price (not to exceed $25,000) for a previously owned "clean" vehicle with a model year at least two years prior to the calendar in which the vehicle is purchased. The credit is not allowed if the lesser of the MAGI for the current or immediately preceding tax year exceeds $150,000 (joint return/surviving spouse), $112,500 (head of household), or $75,000 (individual), as applicable. This credit applies to vehicles acquired between January 1, 2023 and December 31, 2032.

- **Nonbusiness energy property credit** ($12.5 billion) – Extends the credit through December 31, 2032, and changes the credit to 30% of qualified expenditures for energy efficient home improvements. The credit is generally capped at $1,200 per year (up from the current $500), with lower limits for certain types of property. The amendments generally apply to property placed in service after December 31, 2022, but the extension of the credit applies to property place in service after 2021. Product identification numbers will be required for all property placed in service after 2024.
- **Residential energy efficient property credit** ($22 billion) – Extends the credit through December 31, 2034. The applicable percentage of qualified expenditures is 30% for property placed in service between January 1, 2022 and December 31, 2032, and is then phased down to 26% in 2033 and 22% in 2034.

One credit contained in the IRA specifically pertains to small businesses:

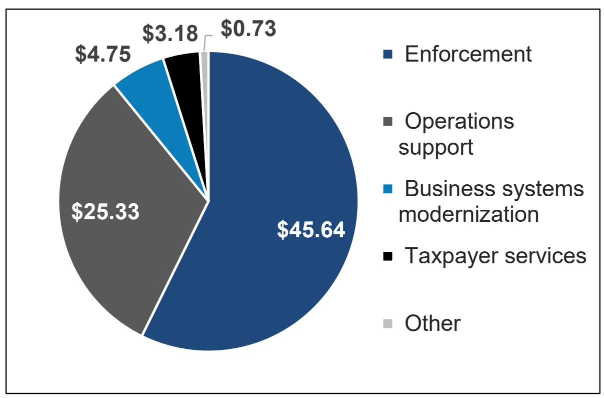
- **Increase in research credit against payroll tax for small businesses** – Doubles the credit for applicable research expenses from the current $250,000 to $500,000 for tax years beginning after December 31, 2022.

In addition, there are a number of new or modified clean energy tax credits and incentives to promote investment in renewable energy and other environmental initiatives. These include:

- Renewable electricity production tax credit ($51 billion)
- Energy investment tax credit ($14 billion)
- Carbon oxide sequestration ($3.2 billion)
- Zero-emission nuclear power production credit ($30 billion)
- Credit for production of clean hydrogen ($13.2 billion)
- Incentives for biodiesel, renewable diesel, alternative fuels ($5.6 billion)
- Incentives for second generation biofuel ($54 million)
- Sustainable aviation fuel credit ($49 million)
- Energy efficient commercial buildings deduction ($362 million)
- New energy efficient home credit ($2 billion)
- Credit for qualified commercial clean vehicles ($3.6 billion)
- Alternative fuel refueling property credit ($1.7 billion)
- Advanced energy project credit ($6.2 billion)
- Advanced manufacturing production credit ($30.6 billion)
- Clean electricity production credit ($11.2 billion)
- Clean electricity investment credit ($50.9 billion)
- Cost recovery for qualified facilities, qualified property, and energy storage technology ($624 million)
- Clean fuel production credit ($2.9 billion)

IRS Funding

Another significant component of the legislation is a considerable increase in funding for the IRS. The IRA has appropriated almost $80 billion in additional funding for the IRS, most of which can be utilized through September 30, 2031. Strikingly, the bulk of the money (57%) is allotted to enforcement efforts, as illustrated below:



In contrast, only 4% was dedicated to improving taxpayer services, even amidst the continuing backlog of processing returns and the inability of taxpayers or tax practitioners to reach the IRS by phone on a timely basis. This demonstrates the focus on using these funds to generate additional tax revenue.

The IRS has indicated that much of the funding will be used to increase staffing, with a focus on hiring and training employees with the necessary skills and expertise to audit high-income taxpayers and corporations. Accordingly, audit rates for these more complex areas are expected to rise in the coming years, though there may be a lag until the appropriate staffing is in place, trained, and ready to be deployed. In fact, the Congressional Budget Office (CBO) estimates the enhanced IRS enforcement will generate over $200 billion in revenue over the ten-year budget period, with almost 80% of that amount generated from 2027 through 2031.

Healthcare Provisions

The other big focus of this legislation relates to healthcare. Key components of the law include:

- **ACA Subsidies** – This legislation extends the enhanced Affordable Care Act (ACA) premium tax credits that were originally enacted by the American Rescue Plan for an additional three years, through the end of 2025. The subsidies otherwise would have expired at the end of this year. The CBO estimates this will cost around $64 billion over the 10-year budget period, inclusive of increased expenditures and reduced revenue.
- **Drug Price Negotiation** – For the first time, the Department of Health and Human Services will be authorized to negotiate prices for certain drugs for Medicare Parts B and D. This will start with 10 high-cost drugs in 2026, increasing to 20 by 2029. The CBO estimates this will reduce Medicare spending by over $100 billion over the 10-year period.
- **Prescription Drug Inflation Rebates** – Starting in 2023, drug manufactures will be required to repay the government if they raise the price of a drug beyond inflation, or face penalties. According to CBO estimates, this will generate around $62 billion.
- **Medicare Part D** – Under the new law, out-of-pocket costs for Medicare Part D drugs will be capped at $2,000 per year starting in 2025 and certain coinsurance amounts will be reduced. The CBO estimates this will result in increased Medicare expenditures of around $25 billion.
- **Other** – The law limits out-of-pocket costs for insulin and certain vaccines for Medicare, Medicaid, and Children's Health Insurance Program (CHIP) beneficiaries.

Other Considerations

JTaylor will continue to monitor additional guidance that may be forthcoming as it relates to the application of the tax provisions included in the Inflation Reduction Act. Should you have questions about how the provisions contained in the recent legislation may impact you or your business, please contact your JTaylor tax advisor. Because the facts and circumstances of each situation are unique and as applicable guidance may continue to evolve, we recommend seeking professional guidance before undertaking actionable steps in regard to these provisions.

Additional Resources:

- Inflation Reduction Act
- Congressional Budget Office, Estimated Budgetary Effects of H.R. 5376, the Inflation Reduction Act of 2022 (August 5, 2022)
- Joint Committee on Taxation, Estimated Budget Effects Of The Revenue Provisions Of Title I – Committee On Finance, Of An Amendment In The Nature Of A Substitute To H.R. 5376, "An Act To Provide For Reconciliation Pursuant To Title II Of S. Con. Res. 14," As Passed By The Senate On August 7, 2022, And Scheduled For Consideration By The House Of Representatives On August 12, 2022 (August 9, 2022)